would be inappropriate; it would be impossible to create rate uniformity without uniformity of programming, a result that is not desirable either to the cable operator or the commercial customer.

Fourth, commercial rates should not be used to offset residential rates. As has been noted, the goal of rate regulation is to set rates at reasonable levels, i.e., those levels that would exist in the presence of effective competition. "Reasonable rate levels" for commercial establishments do not mean the lowest-priced residential cable service that can be attained through offsetting contributions from commercial users. Time Warner agrees with the commenters that the Commission has no authority under the 1992 Cable Act to offset higher commercial rates with even lower residential rates.[49] Indeed, if such offsets are mandated, there would be no benefit in charging higher commercial rates which reflect the increased value to commercial accounts, only to go through the "bookkeeping morass" and "zero-sum game" of adjusting the residential rate downward by the same amount.[50] If the Commission decides to regulate commercial rates, such rates should be set at that level which best emulates a market-driven price. Such determinations should be made independent of the residential rates which formed the basis of the Commission's "benchmark" rate formula.

Finally, if the Commission decides to regulate commercial rates, it should be at the option of local franchising authorities. Congress intended that local franchising authorities control the regulation of basic cable rates.[51] Because there is no evidence of a problem

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[49]See Time Warner Comments at 45; Cablevision Systems Comments at 9; CVI Comments at 19; Rainbow Comments at 6-7.

[50]See NHL Comments at 10.

[51]H.R. Rep. No. 628 at 80.

with the "reasonableness" of commercial rates, cities should not be forced to regulate where they might not desire to do so. In light of the diversity of programming that cable operators provide to individual commercial subscribers, cities may not want to regulate commercial rates because to do so would foreclose cable operators' flexibility in delivering cable service offerings to meet the needs of divergent commercial users. A franchising authority should have the authority to determine whether regulation of commercial cable use would be in its interests.

For the above-stated reasons, Time Warner joins the other commenters in urging the Commission to resist imposing rate regulation on the provision of video services to commercial cable users. However, if the Commission determines that regulation should be imposed on commercial rates, it should be effected at each franchising authority's option, and the rates should be unrelated to, and should not be used to offset, residential rates.

Respectfully submitted,

TIME WARNER CABLE

By ______________________

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Date: July 29, 1994
17456

No. 94-1894

IN THE

United States Court Of Appeals

FOR THE SEVENTH CIRCUIT

TIME WARNER CABLE, a division of
TIME WARNER ENTERTAINMENT COMPANY, L.P.,

Plaintiff-Appellant,

-against-

JAMES E. DOYLE, in his capacity as Attorney General of the State of Wisconsin, and ALAN T. TRACY, in his capacity as Secretary of the Wisconsin Department of Agriculture, Trade and Consumer Protection,

Defendants-Appellees.

ON APPEAL FROM A JUDGMENT OF THE UNITED STATES DISTRICT COURT FOR THE WESTERN DISTRICT OF WISCONSIN

BRIEF AND APPENDIX OF APPELLANT TIME WARNER CABLE

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May 31, 1994

CERTIFICATE OF INTEREST

The undersigned, counsel of record for Time Warner Cable, plaintiff-appellant, furnishes the following list in compliance with Circuit Rule 26.1:

1. The undersigned represents Time Warner Entertainment Company, L.P., of which Time Warner Cable is an unincorporated division, in this appeal.

2. i. Time Warner Inc. manages Time Warner Entertainment Company, L.P., and directly or indirectly owns a majority interest in it.

   ii. US West Cable Corporation, Toshiba American Entertainment, Inc., and Itoshu Entertainment, Inc., are limited partners in Time Warner Entertainment Company, L.P.

3. The law firms of Cravath, Swaine & Moore of New York and Friebert, Finerty & St. John of Milwaukee have appeared for plaintiff-appellant Time Warner Cable in this case.

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TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases **Page(s)**

Cases **Page(s)**

CONSTITUTION

STATUTES

REGULATIONS

LEGISLATIVE HISTORY

MISCELLANEOUS

JURISDICTIONAL STATEMENT

Plaintiff-appellant Time Warner Cable submits this Jurisdictional Statement pursuant to Circuit Rule 28(b).

Jurisdiction of the District Court

The United States District Court for the Western District of Wisconsin had jurisdiction over this action pursuant to 28 U.S.C. § 1331, because the action arises under § 3 of the Cable Television Consumer Protection and Competition Act of 1992, 47 U.S.C. § 543; 47 C.F.R. § 76.981 promulgated thereunder; and the Supremacy Clause, U.S. Const. art. VI, cl. 2.

Jurisdiction of the Court of Appeals

The United States Court of Appeals for the Seventh Circuit has jurisdiction over this appeal from the final judgment of the district court, entered in this action on March 21, 1994, pursuant to 28 U.S.C. § 1291. The Notice of Appeal was filed April 19, 1994.

STATEMENT OF ISSUES

1. Whether the district court erred when it determined that the Federal Communications Commission ("FCC"), acting pursuant to its authority under § 3 of the Cable Television Consumer Protection and Competition Act of 1992 (the "1992 Cable Act"), lacked power to adopt a regulation that would permit cable television operators to continue to charge their subscribers for a limited number of programming services that had been "unbundled" from a group or "tier" of services previously ordered by those subscribers, without resoliciting subscribers to determine if they wished to keep receiving such services; and, if the FCC's rule was valid, whether it preempted application of Wis. Stat. § 100.20 to Time Warner's restructuring of cable service on September 1, 1993.

2. Whether the district court erred in determining that a state law which forbids cable operators to charge their subscribers for a service that subscribers had previously been receiving and paying for was not an effort to regulate "rates for the provision of cable television service" that is prohibited to the states by § 3 of the 1992 Cable Act, 47 U.S.C. § 543(a)(1).

PRELIMINARY STATEMENT

September 1, 1993, marked a turning point in national policy concerning communications via cable television. On that date, operators of cable television systems were expected to come into compliance with an extensive and highly complex regime for regulating cable television rates that had been promulgated in May 1993 by the Federal Communications Commission (the "FCC" or the "Commission"), pursuant to its delegated authority under § 3 of the Cable Television Consumer Protection and Competition Act of 1992 (the "1992 Cable Act"), Pub. L. 102-385, 106 Stat. 1464.[1]

The implementation of rate regulation was an undertaking of enormous proportions. The FCC's Report and Order promulgating its regulations on the subject of cable rates is hundreds of pages long. *See In re Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation*, MM Docket No. 92-266, FCC 93-177, Report and Order and Further Notice of Proposed Rulemaking (adopted April 1, 1993; released May 3, 1993) ("Report and Order") (Tab 1).[2] The FCC's regulations required cable television operators to obtain detailed data and perform complex calculations for virtually all of their systems in order to evaluate and, where necessary, revise their rate schedules in an effort to conform to the new regime. *See, e.g., id.* Appendix D.

In connection with the implementation of the new rate regulation regime, many cable operators determined to rearrange or "restructure" the "tiers" of service that they offered to subscribers.[3] The FCC

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[1] The new rate regulation scheme implemented on September 1 marked a dramatic reversal of congressional policy concerning cable television. Under the prior Federal legislation, the Cable Communications Policy Act of 1984, Pub. L. 98-549, 98 Stat. 2788, regulation of cable rates was generally prohibited.

[2] For the Court's convenience, copies of the FCC materials cited in this brief are included in the Volume of FCC Materials submitted herewith. The references to Tab numbers are to tabs in that Volume.

[3] Cable operators usually offer to their subscribers two levels or "tiers" of service, each consisting of a group of programming services.

encouraged cable operators to restructure in this fashion, and it used its broad powers under the 1992 Cable Act to clear away many perceived obstacles to that process, which it regarded as essential for inauguration of the new regime, *see* pp. 11-13, *infra*. For example, on June 15, 1993, recognizing that cable operators faced a herculean task that had great potential for disruption of service to subscribers, the FCC extended the compliance date for its cable rate regulations from June 21, 1993, to October 1, 1993. *See In re Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation*, MM Docket No. 92-266, FCC 93-304, 58 Fed. Reg. 33,560 (adopted and released June 15, 1993) ("June Order") (Tab 2). (Later, however, the Commission accelerated the compliance date by 30 days to September 1, greatly increasing the strains upon operators, *see In re Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation*, MM Docket No. 92-266, FCC 93-372, 58 Fed. Reg. 41,042 (adopted and released July 27, 1993) ("July Order") (Tab 4).) As discussed below, the FCC also preempted the application of state laws that had potential to interfere with the restructuring process.

Like other cable operators, on September 1, 1993, plaintiff-appellant Time Warner Cable ("Time Warner"), a division of Time Warner Entertainment Company, L.P. ("TWE"), and the second largest cable operator in the United States, restructured its cable service in the areas where it does business. This appeal arises from an administrative proceeding commenced on August 31, 1993, by defendant-appellee James E. Doyle, the Attorney General of Wisconsin, before the Wisconsin Department of Agriculture, Trade

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Federal law requires all subscribers to subscribe to the first level of service, which is usually called the "basic" tier, and also specifies the minimum content of that tier. 47 U.S.C. § 543(b)(7)(A). Subscription to the second level, usually called the "standard" tier, is optional. The great majority of subscribers, however, subscribe to both the basic and the standard tiers. (Affidavit of Thomas Sharrard, sworn to November 22, 1993 ("Sharrard Aff.") ¶ 3, A23)

Citations in the form "A __" refer to the Appendix to this Brief.

and Consumer Protection (the "Agriculture Department"), of which defendant Alan T. Tracy is the Secretary, charging Time Warner with violating a provision of Wisconsin law in connection with the September 1 restructuring of its cable service in its cable systems in Milwaukee, Wisconsin, and two smaller cities.

As part of its September 1 restructuring in each of the Wisconsin systems in question, Time Warner "unbundled" three or four programming services (*e.g.*, E! Entertainment Television and The Discovery Channel) that had previously been available only as part of a tier of services and offered them on what is known as an "a la carte" basis. There was no change in price or number of channels. As a result of this unbundling, subscribers could separately drop or keep the services in question if they wished.

Wisconsin contended that even though these "a la carte" services were already being provided to subscribers as part of the cable service they had ordered, Time Warner was required to seek each subscriber's assent again if it wished to continue to charge for the services, and that Time Warner's failure to confirm subscribers' continued desire to receive the services constituted an improper "negative option" under Wisconsin's "unfair trade practices" statute, Wis. Stat. § 100.20. Time Warner, however, believed that FCC regulations regarding negative options, with which it had complied, preempted the Wisconsin law.

Adopting a point of view not briefed or argued by either side, the court below concluded that if the applicable FCC regulation permitted Time Warner to charge for the unbundled programming services without resoliciting its subscribers, then the regulation was invalid under the "plain meaning" of a provision of the 1992 Cable Act dealing with negative options, 47 U.S.C. § 543(f), which prohibits charges for service or equipment not "affirmatively requested by name". Accordingly, the court ruled that the regulation could not have preemptive force. In reaching this conclusion, which was illogical and impractical, the court did not consider any of the policy issues examined by the FCC in formulating its rules or of the scope of the FCC's powers in the cable field. The court also held that Wisconsin was not using its unfair trade practices statute to regulate cable rates in a fashion forbidden by § 3 of the 1992 Cable Act.

The district court's analysis was highly formalistic—and just wrong. Contrary to the Supreme Court's directive in *Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 842-43 (1984), the court did not ask whether Congress had "directly addressed the precise question at issue" (it had not), but instead "simply impose[d] its own construction on the statute". *Id.* at 843. This was error. The statute does not and logically could not have the "plain meaning" the district court ascribed to it. Because the statutory language did not resolve the issue, the district court was required to proceed to the second stage of the *Chevron* analysis, asking whether the agency adopted "a permissible construction of the statute". *Id.* The regulation was valid under the *Chevron* test, and it preempted the Wisconsin law. The district court's conclusion that Wisconsin had not attempted to engage in regulation of cable rates was also unsound.

This appeal raises one additional matter. The FCC's pronouncements when it promulgated its negative option rule showed an unmistakable intent to preempt state law. Shortly after the judgment below was entered, however, the Commission, acting "on reconsideration on our own motion" following the appointment of a new Chairman, purported to "substitute" a new analysis for its earlier statements. *In re Implementation of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, Buy-Through Prohibition*, MM Docket Nos. 92-266 and 92-262, Third Order on Reconsideration (adopted February 22, 1994; released March 30, 1994) ("Third Order on Reconsideration") ¶ 126 (Tab 7). As we show below, there is no reason to regard the statements in the Third Order on Reconsideration as having any bearing on preemption of the Wisconsin statute as sought to be applied to Time Warner's September 1 restructuring. As we also show, the FCC's recent pronouncements could not be given retroactive effect in any event.[4]

[4] The district court did not consider the new FCC analysis, which was not released until after judgment was entered. We believe that the issues presented by the Third Order on Reconsideration are primarily legal and can be addressed by this Court. Alternatively, if the Court determines that the district court should consider those issues in the first instance, then the judgment appealed from should be vacated and the matter should be remanded for that purpose.

STATEMENT OF THE CASE

A. Background: The Statutory Scheme and Its Implementation

1. A la Carte Services and Negative Options

Section 3 of the 1992 Cable Act, 47 U.S.C. § 543, establishes a complex regime for regulating most cable operators' rates for most cable programming services.[5] Section 3 expressly provides that "[n]o Federal agency or State may regulate the rates for the provision of cable service" except as expressly provided thereunder. *Id.* § 543(a)(1). Section 3 does not, in fact, create any role for the States in the field of rate regulation, but generally leaves such regulation in the hands of local franchising authorities and the FCC.

In essence, rates for so-called "basic" service, which Federal law dictates must include certain broadcast channels and certain public, educational and governmental channels, *see* 47 U.S.C. § 543(b)(7), are subject to regulation by municipal franchising authorities pursuant to regulations prescribed by the FCC, with the FCC able to regulate basic rates directly in certain circumstances, *see id.* § 543(a), (b). Rates for "cable programming services", a term that encompasses all

[5] Rate regulation may be imposed upon cable systems that are not subject to "effective competition", a term defined in the statute in such a way, *see* 47 U.S.C. § 543(*l*)(1), as to ensure that almost all cable operators may be subject to rate regulation.

TWE has challenged the constitutionality of § 3 and several other provisions of the 1992 Cable Act. *See Daniels Cablevision, Inc. v. United States*, 835 F.Supp. 1 (D.D.C. 1993), *appeal pending*, No. 93-5290 (D.C. Cir. 1993); *see also Turner Broadcasting System, Inc. v. FCC*, 819 F. Supp. 32 (D.D.C. 1993) (3 judge court), *appeal pending*, No. 93-44 (U.S. 1993). TWE has also commenced proceedings in the United States Court of Appeals for the District of Columbia Circuit to obtain judicial review of various FCC actions taken pursuant to the Act, including the Report and Order. *See, e.g., Time Warner Entertainment Co., L.P. v. FCC*, No. 93-1723 (D.C. Cir. 1993); *Time Warner Entertainment Co., L.P. v. FCC*, No. 93-1727 (D.C. Cir. 1993).

video programming services except those that are included in the basic tier or offered on a per-channel or per-program basis, are subject to regulation only by the FCC. *See id.* § 543(c)(1)(A).

Rates for program services that are "offered on a per-channel or per-program basis" are exempt from any form of rate regulation. *See id.* § 543(c)(2)(D) (exempting such services from definition of regulated "cable programming services"). The a la carte services at issue here are offered on a per-channel basis and so are not subject to rate regulation.

One reason Congress exempted such per-channel, a la carte services from rate regulation was to encourage operators to "unbundle" their tiered offerings. *See* Report and Order ¶ 327 ("the rationale underlying Congress's decision" to exempt per-channel services from rate regulation was to encourage "greater unbundling of offerings"). As stated in the Senate Report, Congress believed that "greater unbundling of offerings leads to more subscriber choice and greater competition among program services". S. Rep. No. 92, 102d Cong., 1st Sess. 77 (1991) ("Senate Report"); *see also* H.R. Rep. No. 628, 102d Cong., 2d Sess. 90 (1992) (per channel offerings "can enhance subscriber choice"). The legislative history makes clear that greater unbundling of service offerings is a significant objective of the 1992 Cable Act:

> "In sum, one of the prime goals of the legislation is to enhance subscriber choice. Unbundling is a major step in this direction. Cable operators and programmers are urged to work toward this objective, while also seeking to accomplish other legitimate goals." Senate Report at 77.

Congress evidently intended the exemption from rate regulation as an incentive to greater unbundling.

The FCC released its Report and Order, the first comprehensive set of rules and regulations under the rate regulation provisions of the 1992 Cable Act, in May 1993.[6] The Report and Order sets forth

[6] In essence, the FCC adopted a system of "benchmark" ratemaking, under which permissible rates for regulated service are determined by comparison to rates in cable systems of comparable

certain conclusions concerning the unbundling of programming services and the treatment of such unregulated a la carte services. The Commission rejected an argument that cable operators should be prohibited from unbundling tiered services to offer them on an unregulated a la carte basis, stating that "[w]e also do not believe that anything in the Act requires us to restrict movement of a channel to premium and deregulated status". *Id.* ¶ 441 n.1105. In addition, pursuant to its authority to promulgate regulations to "prevent evasions" of § 3 of the Act, *see* 47 U.S.C. § 543(h), the FCC declined to determine, "in the absence of a particular factual context", whether "a shift of programming from a tier to an 'a la carte offering' in and of itself would constitute evasion". Report and Order ¶ 453 n.1161.

The Commission also determined that cable operators should be permitted freely to offer unregulated a la carte services in collective offerings or "packages", so long as the price for the package did not exceed the sum of the a la carte prices and the services included in the package could in fact be purchased separately. *Id.* ¶¶ 327-328. The FCC specifically stated that "we believe cable operators should be free to offer collective offerings at a combined price which is less than the sum of the charges for the individual services", because "such discounts benefit the consumer". *Id.* ¶ 327. The Commission reasoned that subjecting such collective offerings to regulation could be "counterproductive" because operators "likely will refrain from making such offerings" if they are treated as regulated tiers, a result which could "disadvantage consumers" by "denying them discounts" and "by limiting subscriber access to a greater quantity of premium programming". *Id.* ¶ 329.[7]

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size that are subject to "effective competition", as defined, which are used as benchmarks. The ratemaking analysis ultimately yields a price per channel that the particular cable system is permitted to charge. *See* Report and Order ¶¶ 207, 396. The "benchmark" price is then subject to a price "cap", *i.e.*, it may not be increased by more than an amount set by the FCC's regulations. *Id.* ¶¶ 227, 396.

[7] The FCC recently revisited its a la carte policies, adopting new "interpretive guidelines" pursuant to its statutory duty to regulate "evasions" of rate regulation, 47 U.S.C. § 543(h). *See In re*

As an integral part of the Federal rate regulation scheme, § 3 of the 1992 Cable Act also provides that "[a] cable operator shall not charge a subscriber for any service or equipment that the subscriber has not affirmatively requested by name". 47 U.S.C. § 543(f). This provision was included in the statute in response to a situation in which another cable operator added a newly-created "per channel" program service to its channel line-up and then proceeded to charge extra for receiving the channel, even though it had never previously formed part of the services ordered by subscribers. *See* 137 Cong. Rec. S7047-48 (daily ed. June 4, 1991) (statement of Sen. Gorton).

The FCC addressed the negative option provision at length as part of its rate regulation proceeding. The Commission perceived that, if interpreted with excessive literality, the negative option provision could be said to come into play with respect to *any* change in service, however trivial. Recognizing that the statutory language "applies to 'any service'", the FCC noted that the legislative history clarifies that the provision "does not apply to changes in the mix of programming in a tier". Report and Order ¶ 440, discussing H.R. Conf. Rep. No. 862, 102d Cong., 2d Sess. 65 (1992) ("Conference Report"). While operators would be prohibited from adding, at additional cost to subscribers, "new" services which subscribers have yet to "actually receive", the FCC opined that Congress did not intend the negative option prohibition to apply to "change[s] in the mix of channels" or "additions or deletions of channels" unless such changes altered the

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Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation, Second Order on Reconsideration, Fourth Report and Order, and Fifth Notice of Proposed Rulemaking, MM Docket No. 92-266, FCC 94-38 (adopted February 22, 1994; released March 30, 1994) ¶¶ 191-200 (Tab 6). Nonetheless, the FCC affirmed its policy that "the public interest will be served by generally permitting nonregulated treatment of collective offerings of 'a la carte' channels if the offering enhances consumer choice and does not constitute an evasion of rate regulation". *Id.* ¶ 194.

"fundamental nature" of the service the subscriber had originally ordered. *Id.*[8]

Similarly, the FCC concluded that, barring some "fundamental change", "restructuring of tiers and equipment, including restructuring appropriate for implementing the Cable Act's provisions", would not violate the negative option prohibition so long as "subscribers will continue to receive the same number of channels and the same equipment". *Id.* ¶ 441. The Commission concluded that, where such is the case, "a subscriber presumably has already 'affirmatively requested' this level of service". *Id.*

Accordingly, as part of its Report and Order, the FCC promulgated a rule concerning negative options, which restated the basic statutory prohibition, but also provided:

> "[t]his provision . . . shall not preclude the addition or deletion of a specific program from a service offering, the addition or deletion of specific channels from an existing tier of service, or *the restructuring or division of tiers of service that do not result in a fundamental change in the nature of an existing service or tier of service* provided that such change is otherwise consistent with applicable regulations". 47 C.F.R. § 76.981 (emphasis added).

In the FCC's rate regulation proceeding, several municipalities submitted comments arguing that state and local authorities should retain power to enforce state and local laws concerning negative options against cable operators, notwithstanding the Federal statutory prohibition and the FCC's intention to promulgate a negative option rule. Report and Order ¶ 439. In its Report and Order, the FCC expressly rejected that suggestion, stating that any state or local regulation would be limited and could not be more stringent than the Federal regulation:

> "[s]ome municipalities argue that state and local governments should have concurrent enforcement powers over negative option billing practices. . . . We do not preclude state and local authorities from adopting rules or taking enforcement action relating to basic services or associated equipment *consistent with the implementing rules we adopt. . . .*" *Id.* ¶ 439 n.1095 (emphasis added).

Thus, state and local authorities could regulate negative options only with respect to basic services and associated equipment, and only if they did so in a manner consistent with the FCC's rules. Otherwise, Federal regulation would be exclusive.

[8] As an example of a "fundamental change", the FCC suggested that deleting all channels in a tier and replacing them with different services would not be permissible. Report and Order ¶ 440 n.1100.

2. Implementation of the Statutory Scheme

The FCC was well aware that implementing its rate regulations (and its regulations under various other provisions of the Act) would lead cable operators to restructure their services, often extensively; indeed, it encouraged them to do so. Its proceedings consistently reflect its concern with facilitating the process and clearing away possible obstacles to implementation of the statutory scheme.

For example, "recogniz[ing] that rate regulation of cable service imposes significant new obligations on cable operators", the FCC on June 15, 1993, extended the time for operators to come into compliance with its new regulations from June 21, 1993, to October 1, 1993, observing that the extension of time would give "operators greater opportunity to ensure a smooth transition to rate regulation". June Order, 58 Fed. Reg. 33,560 (Tab 2). On July 27, 1993, however, less than six weeks later and little more than 60 days before the extended compliance date, the FCC, in response to congressional pressure, ordered that the effective date for its cable regulations be accelerated to September 1, 1993. July Order, 58 Fed. Reg. 41,042 (Tab 4).

The FCC's First Order on Reconsideration in its rate regulation proceeding, *In re Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation*, MM Docket No. 92-266, FCC 93-428, First Order on Reconsideration, Second Report and Order and Third Notice of Proposed Rulemaking (adopted and released August 27, 1993) ("First Order on Reconsideration") (Tab 5), underscores the Commission's recognition that cable operators were under immense operational pressure to meet the accelerated September 1, 1993 deadline. Taking the unusual (but necessary) step of making its policies in its First Order on Reconsideration effective immediately (in time for the September 1 deadline), the FCC noted that "[i]t is important that these [regulatory] changes go into effect as soon as practical, in order to facilitate compliance of cable operators with the 1992 Cable Act and the Commission's implementing regulations, which go into effect September 1, 1993". First Order on Reconsideration ¶ 3.[9] As one step toward facilitating restructuring, the FCC preempted state and local (and waived its own) notice requirements with respect to tier restructuring for the express reason that "notice requirements . . . in state or local laws or regulations could make it practically impossible for cable operators to meet such notice obligations, while at the same time implementing required rate adjustments". July Order, 58 Fed. Reg. at 41,043 (¶ 6).

In the First Order on Reconsideration, the FCC also clarified its intention to preempt any and all state or local regulation of negative options in connection with cable operators' initial restructuring to come into compliance with the new rate regulations. The Commission affirmed that "franchising authorities may not regulate tier restructuring in a manner that is inconsistent with the 1992 Cable Act". *Id.* ¶ 86 n.127. It went on to add that "[i]n particular, local

[9] Rate regulation was not the only area where the rapid pace at which the 1992 Cable Act was implemented placed strains upon cable operators and created potential for service disruption and subscriber confusion. For example, the "must carry" provisions of the 1992 Cable Act, which required cable operators to offer particular broadcast television stations on particular channels on their systems, often displacing other programming selected by the operator, were an additional source of significant logistical stresses, as operators scrambled to revise their channel lineups. The FCC decided to delay the deadline for compliance with its must carry rules until October 6, 1993, since "this approach will be the least disruptive to subscribers and will ensure an orderly transition to retransmission consent". *In re Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Rate Regulation,* MM Docket No. 92-259, FCC 93-354, 58 Fed. Reg. 40,366, 40,367 (adopted July 15, 1993; released July 16, 1993) (Tab 3).

authorities are *precluded from regulating negative option billing to prevent tier restructuring* regardless of how the local requirement is characterized". *Id.* (emphasis added).

B. Time Warner's Restructuring and Wisconsin's Response

On September 1, 1993, as the new FCC rate regulations went into effect, Time Warner restructured its service offerings in its various cable systems, including its systems in the City of Milwaukee and two smaller cities.[10] Time Warner changed the prices of its basic and standard tiers in order to bring them into compliance with the FCC's rate regulations. In each of the Wisconsin systems that are at issue in this litigation, Time Warner also "unbundled" three or four programming services that had previously been included in groups or "tiers" of services and made them available both separately and in a discounted "package", so that subscribers could decline to take some or all of the services if they wished. Other than placing these services on such an "a la carte" footing, however, there was no change in service if subscribers took no action. Milwaukee subscribers continued to receive the same number of channels they had originally ordered, with the same programming services, at the same price.[11]

On August 31, 1993, the day before Time Warner's restructuring was to go into effect, defendant Doyle filed a Complaint and Request

[10] The Time Warner cable systems involved in this appeal are those operating in the City of Milwaukee and in the cities of Brookfield and Plymouth-Dacada, Wisconsin.

[11] The details of Time Warner's service structure and pricing both before and after the September 1, 1993 restructuring are set forth in Sharrad Aff. ¶¶ 5-16, A23-25.

Time Warner promptly notified its subscribers of the changes in its service—and of the fact that they now had the option of dropping some or all of the a la carte services—through various means, including mailings and announcements over the cable system. Subscribers who cancelled one or more of the a la carte services received full credit retroactive to September 1, 1993. (Sharrard Aff. ¶¶ 17-23, A25-26) for Expedited Hearing (the "Administrative Complaint") against Time Warner before the Agriculture Department. (*In re Trade Practices of Time Warner Entertainment, L.P.*, Docket No. 2490) (A18) The Administrative Complaint alleged that by continuing to charge subscribers for the a la carte channels without confirming that subscribers wished to continue receiving them, Time Warner had engaged in "unfair trade practices and unfair methods of competition" within the meaning of Wis. Stat. § 100.20. (Administrative Complaint at 3) The Administrative Complaint sought injunctive relief and "disgorgement" of moneys paid by subscribers to Time Warner for the a la carte channels. (*Id.* at 4)

C. The Proceedings Below

On September 21, 1993, Time Warner commenced an action for declaratory and injunctive relief in the United States District Court for the Western District of Wisconsin, seeking a ruling that Wis. Stat. § 100.20 had been preempted insofar as it might apply to Time Warner's September 1 restructuring. Thereafter, the parties agreed to a stay of the Agriculture Department proceeding, pending resolution of the preemption issue. (Stipulation and Agreement for Stay of Proceedings and Implementation Order (Oct. 26, 1993), attached as Exhibit B to Time Warner Cable's Proposed Findings of Fact, dated Nov. 22, 1993) The defendants answered the Complaint on October 11, 1993.

On November 22, 1993, Time Warner moved for summary judgment, contending that the FCC had preempted statutes such as Wis. Stat. § 100.20 through its negative option regulation. Time Warner also challenged the Wisconsin action as expressly preempted by the provisions of § 3 of the 1992 Cable Act, which provide in pertinent part, that "[n]o Federal agency or State may regulate the rates for the provision of cable service" except as provided in 47 U.S.C. § 543(a)(1) and 47 U.S.C. § 532. Defendants opposed Time Warner's motion, arguing primarily that the FCC lacked power to preempt state laws concerning negative options.

In an Opinion and Order dated March 17, 1994 ("Opinion"), the district court ruled for defendants. Taking a view of the case that had not been urged or briefed by the parties, the court concluded that if the FCC's negative option regulation authorized the manner in which

Time Warner carried out its restructuring (as it plainly did), then the regulation was invalid under the plain meaning of the "by name" language contained in the statute and so lacked any preemptive force. (Opinion at 15, A12)[12] In the court's view, the "express language" of the statute would not "permit a cable operator to charge for a service that at one time was part of a tier the customer requested by name" if the programming service was not also "requested by name itself". (Opinion at 14, A11)

The court also determined that the proposed application of Wis. Stat. § 100.20 did not constitute impermissible rate regulation. The court reasoned, first, that the injunctive relief requested by Wisconsin in the Agriculture Department proceeding "would have the effect of setting plaintiff's a la carte channel rates at zero in the future only if plaintiff continued to provide those channels free of charge to those subscribers who did not place affirmative orders for the channels". (Opinion at 19, A15) Although the court found "[c]ompelling plaintiff to disgorge funds already collected" to be "slightly more problematic", it ruled that equating such a monetary remedy with rate regulation would "exal[t] form over substance" because "[d]efendants could avoid this objection if instead of seeking disgorgement, they requested and imposed a fine equal to the amount collected by plaintiff from the recipients of a la carte services". (Opinion at 20, A15)

Having determined each of these issues in defendants' favor, the court denied Time Warner's motion for summary judgment and, on March 21, 1994, entered judgment for defendants. (Judgment, A1)

Time Warner timely filed its Notice of Appeal on April 19, 1994.

[12] Looking outside of the rate regulation provision to 47 U.S.C. § 552(c)(1), which provides that "[n]othing in this subchapter shall be construed to prohibit any State or any franchising authority from enacting or enforcing any consumer protection law, to the extent not specifically preempted by this subchapter", 47 U.S.C. § 552(c)(1), the court also suggested that the FCC's negative option rule could not have preempted the Wisconsin statute because the text of the rule itself (as opposed to the FCC's commentary in the Report and Order) did not address the subject of preemption. (Opinion at 18, A13)

ARGUMENT

I. THE FCC'S NEGATIVE OPTION RULE IS VALID AND PREEMPTS STATE LAW.

The district court concluded that the FCC's negative option rule was not authorized by the 1992 Cable Act and, therefore, could not preempt state law. In this section, we show, first, that the FCC's rule was well within its powers and, second, that the rule preempted the Wisconsin statute. We then show that the FCC's recent statements about preemption of state negative option laws were not intended to, and could not, affect the result here.

Because the court below ruled on motion for summary judgment, its judgment is subject to review *de novo* in this Court. *DRL Enterprises v. United States*, No. 93-2631, 1994 WL 201435 (7th Cir. May 24, 1994); *Lett v. Magnant*, 965 F.2d 251, 255 (7th Cir. 1992).

A. The Court Below Erred in Holding That the FCC Lacked Power to Promulgate Its Negative Option Rule.

In reviewing an executive agency's regulation challenged as contrary to the underlying statute, a court puts the regulation to the two-part test crafted by the Supreme Court in *Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984). The court considers, first, "whether Congress has directly spoken to the precise question at issue"; if it has, the congressional directive must be followed. *Id.* at 842. If Congress "has not directly addressed the precise question at issue", however, then the court "does not simply impose its own construction on the statute", but determines "whether the agency's answer" to the particular issue "is based on a permissible construction of the statute". *Id.* at 843.

In reaching the conclusion that the FCC lacked power to promulgate its negative option rule, the court below did not appropriately apply the *Chevron* analysis. The court did not focus upon whether Congress had "directly spoken to the precise question at issue" (467 U.S. at 842), which was whether, in order to continue to charge for a particular programming service (or a package of such services), a cable operator must receive separate reconfirmation of each subscriber's desire to continue receiving that service once it is

unbundled from an existing service tier and made available on an a la carte basis. Rather, the court simply applied its own view of the "plain meaning" of the words "by name". But the meaning of the statute was anything but "plain", and the court should have proceeded to the second prong of the *Chevron* test. If it had, it would have seen that the FCC's resolution of the issue presented was eminently reasonable.

The court below read the phrase "by name" to mean "by the proper name of the particular service in question". *See* Opinion at 14, A11 (statute "requires a cable operator to obtain a request for a *given service by name*") (emphasis added). Under the district court's reading, an operator could not "charge for a service that at one time was part of a tier the customer requested by name" unless and until that particular service was "requested by name itself". *Id.*

The district court's reading leads to results that are demonstrably absurd and not intended by Congress, results which (as we later show) the FCC specifically anticipated and meant to avoid. For example, under the district court's construction, a cable operator that offered a tier called "Standard Service" consisting of 30 channels would be required to resolicit all of its subscribers if, as a means of enhancing subscriber flexibility, it divided the existing tier and began to market two separate 15-channel tiers (consisting of the same services and offered at the same aggregate price) called "Standard Service" and "Preferred Service".[13] Indeed, under the district court's interpretation, if the operator dropped the name "Standard Service" and marketed the new 15-channel tiers under catchier names—"Cable Silver" and "Cable Gold"—it would not be able to charge for *either* tier until it had resolicited all subscribers.

The absurdity of the district court's reading is also shown by its application to cable equipment, to which the negative option provision also applies. Prior to implementation of the FCC's rate regulations, cable operators typically did not make separate charges for items of

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[13] This would follow because, as the district court noted (Opinion at 13, A10), the term "service" is not defined as it is used in the negative option provision and would appear to apply to tiers of service as well as to individual programming services.

equipment, such as converters that are needed in order to receive cable service.[14] Rather, the price of such equipment was included in the price of the cable subscription. Under the FCC's rate regulations, however, operators were required to unbundle equipment charges as separate items on subscriber bills. *See* Report and Order ¶¶ 284-88. If the "by name" requirement meant "by the proper name of the particular service [or equipment] in question", then cable operators would have been required to resolicit all of their subscribers before beginning to make separate charges for converter boxes and other equipment items, which most subscribers had never ordered "by name" in the sense used by the district court. Nothing in the statute required such an exercise, and the district court erred in concluding that it did.

Particularly in the context of the enabling legislation for complex regulatory schemes, seemingly simple language often does not readily reveal an unmistakable "intent of Congress", which is a court's touchstone in weighing the validity of administrative rulemaking. *See, e.g.*, *Hanson v. Espy*, 8 F.3d 469, 474 (7th Cir. 1993) (meaning of "person" not clear); *Helea v. Bowen*, 871 F.2d 48, 50 (7th Cir. 1988) (meaning of "received" not clear); *Texas Utilities Electric Co. v. FCC*, 997 F.2d 925, 929-32 (D.C. Cir. 1993) (meaning of "cable television system" ambiguous). This Court has emphasized the need to remain "mindful that in ascertaining the plain meaning of a statute, the court must look not only to the particular statutory language at issue, but to the language and design of the statute as a whole". *Milwaukee Gun Club v. Schulz*, 979 F.2d 1252, 1255 (7th Cir. 1992). To quote Learned Hand, "[w]ords are not pebbles in alien juxtaposition"; they "take their purport from the setting in which they are used". *NLRB v. Federbush Co.*, 121 F.2d 954, 957 (2d Cir. 1941). Isolated words removed from their context do not reveal "plain meaning". As this Court has stated, "First, the plain language rule *does not apply to parts of sentences*. Second, context is important to explain the meaning of otherwise intelligible terms, especially when referring to

[14] A converter is a device, usually placed on top of the subscriber's television set, that converts the signal carried over the cable system (which is often "scrambled" to prevent theft) to one that the television set can display.

a complicated and highly technical [statute]". *Harco Holdings, Inc. v. United States*, 977 F.2d 1027, 1030 (7th Cir. 1992) (emphasis added; citation omitted). And if the Cable Act's negative option provision had the "plain meaning" the district court ascribed to it (and it does not), "where literal application of a text would lead to absurd results or thwart the obvious intentions of its drafters, 'those intentions must be controlling'". *Marlowe v. Bottarelli*, 938 F.2d 807, 812 (7th Cir. 1991) (quoting *Griffin v. Oceanic Contractors Inc.*, 458 U.S. 564, 571 (1982)).

In adopting its "plain meaning" analysis, the district court "simply impose[d] its own construction on the statute" in precisely the manner forbidden by *Chevron*. 467 U.S. at 843. If the district court had proceeded to the second prong of the *Chevron* analysis (as it should have)—determining whether "the agency's answer" to the particular issue "is based on a permissible construction of the statute"—it would have been compelled to uphold the Commission's regulation.

As the Supreme Court has observed, implementing a complex regulatory program "necessarily requires the formulation of policy and the making of rules to fill any gap left, implicitly or explicitly, by Congress". *Morton v. Ruiz*, 415 U.S. 199, 231 (1974). Agencies authorized by Congress to implement and administer regulatory schemes may not only determine the meaning of statutes, but also their "reach", where Congress has not specified it. *United States v. Shimer*, 367 U.S. 374, 382 (1961) (*quoted in Chevron*, 467 U.S. at 844-45). And where the agency must "reconcil[e] conflicting policies" manifested by a statutory scheme, the agency's resolution of such conflicts is treated with deference, especially where "a full understanding of the force of statutory policy in the given situation has depended upon more than ordinary knowledge respecting the matters subjected to agency regulations". *Shimer*, 367 U.S. at 382. So long as the agency's "choice represents a reasonable accommodation of conflicting policies that were committed to the agency's care by the statute", a reviewing court "should not disturb it unless it appears from the statute or its legislative history that the accommodation is not one that Congress would have sanctioned". *Id.* at 383 (quoted in *Chevron*, 467 U.S. at 845).

In excepting from its negative option rule "the restructuring or division of tiers of service that do not result in a fundamental change in the nature of an existing service or tier of service", 47 C.F.R. § 76.981, the FCC made exactly the sort of "reasonable accommodation of conflicting policies" that is "committed to the agency's care" by the Communications Act. *Shimer*, 367 U.S. at 383; *accord Chevron*, 467 U.S. at 845.

The FCC recognized that there was tension between the congressional directives to establish a comprehensive rate regulation regime and encourage cable operators to unbundle their tiered services, on the one hand, and the prohibition against negative options on the other hand, and that this tension in the statutory policies was likely to be heightened in connection with the restructuring of tiers at the inception of the new rate regulation scheme. *See* Report and Order ¶¶ 440-41. The FCC's negative option rule, and particularly its exception for service changes undertaken in connection with restructuring that do not result in a "fundamental change" in service, represented a carefully considered effort by the Commission to resolve this tension in the statutory directives. *See* pp. 7-11, *supra*. As the FCC perceived, if the statute were construed to require a fresh solicitation in order to assure the operator's continued ability to charge its customers any time there was such a minor change in the content or structure of cable service, then cable operators would resolicit their subscribers more or less constantly. Report and Order ¶ 440. The Commission had good grounds and ample power to reject such a formalistic approach, which would have little utility from any reasonable consumer protection standpoint and would impose enormous burdens on cable operators.

The court below also failed to acknowledge the breadth of the FCC's powers under the Communications Act of 1934, of which the 1992 Cable Act is a part. As the Supreme Court has repeatedly recognized, Congress has entrusted the FCC with the stewardship of national communications policy. *See Capital Cities Cable, Inc. v. Crisp*, 467 U.S. 691, 699-700 (1984); *United States v. Southwestern Cable Co.*, 392 U.S. 157, 167-68 (1968). As the Court has stated, in the cable area as well as elsewhere, "the Commission's authority extends to all regulatory actions 'necessary to ensure the achievement of the Commission's statutory responsibilities'". *Crisp*, 467 U.S. at 700 (quoting *FCC v. Midwest Video Corp.*, 440 U.S. 689, 706 (1979)).

Pursuant to the Communications Act of 1934, Congress has provided the FCC with broad powers to make and implement necessary rules and regulations.[15] In the specific context of cable television regulation, Congress has authorized the FCC to promulgate comprehensive regulations concerning such matters as rates for cable service and equipment and a host of other subjects.[16] With respect to rate regulation, Congress specifically directed the FCC to formulate regulations that would "reduce the administrative burdens on subscribers, cable operators, franchising authorities, and the Commission". 47 U.S.C. § 543(b)(2)(A). Congress also generally authorized the FCC to promulgate "standards, guidelines, and procedures concerning the implementation and enforcement of [its rate] regulations", *id.* § 543(b)(5), and to establish "procedures by which cable operators may implement" those regulations, *id.* § 543(b)(5)(A); *see also id.* § 543(c)(1)(B). And the statute authorized the FCC to "establish standards, guidelines, and procedures to prevent evasions, including evasions that result from retiering, of the requirements of this section". *Id.* § 543(h).

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[15] As a general matter, Section 303(r) of the Communications Act authorizes the FCC to "[m]ake such rules and regulations and prescribe such restrictions and conditions, not inconsistent with law, as may be necessary to carry out the provisions of this Chapter". 47 U.S.C. § 303(r). Similarly, § 154(i) of the Act provides that "the Commission may perform any and all acts, make such rules and regulations, and issue such orders, not inconsistent with this Chapter, as may be necessary in the execution of its functions". *Id.* § 154(i).

[16] *See, e.g.*, 47 U.S.C. § 543(b)(1) (FCC to establish regulatory structure for local and Federal regulation of basic cable rates); *id.* § 543(b)(5) (FCC to establish "standards, guidelines, and procedures" concerning "implementation and enforcement" of rate regulation, including, "procedures by which cable operators may implement" rate regulations); *id.* § 543(c)(1) (FCC to establish regulatory structure for "cable programming services"); *id.* § 534(f) (FCC to implement "must carry" provisions concerning carriage of commercial broadcast stations by cable systems); *id.* § 544a(b) (FCC to prescribe rules concerning consumer electronics equipment compatibility); *id.* § 552(b) (FCC to establish customer service standards).

Standing alone, without reference to any of its other powers, the FCC's power to prescribe regulations to "prevent evasions" amply justified and completely supported its adoption of the negative option rule. Under this provision, the FCC has power to prevent any "evasion" of any of the provisions of "this section"—*i.e.*, of § 3 of the Act, 47 U.S.C. § 543, which includes the negative option provision, codified at *id.* § 543(f). Thus, the FCC necessarily has power to determine not only what constitutes an evasion of the negative option provision, but also *what does not.*

Under *Chevron*, an agency rule will be upheld unless it is "manifestly contrary to the statute", 467 U.S. at 844, or the agency's resolution of an issue "'is not one that Congress would have sanctioned'", *id.* at 845 (quoting *Shimer*, 367 U.S. at 383). The construction adopted by the agency need not have been "the only one it permissibly could have adopted" nor even the one the reviewing court would choose were it standing in the agency's shoes. *Id.* at 843 n.11. As this Court has put it, "judges must police the boundaries of an agency's statutory authority", but within those broad boundaries must "leave policy-making to the policy-makers appointed by Congress". *Homemakers North Shore, Inc. v. Bowen*, 832 F.2d 408, 412 & n.1 (7th Cir. 1987). Here, it cannot be said that the FCC's negative option rule contravened congressional intent. The rule was, therefore, perfectly valid, and the district court was wrong to strike it down.

B. The FCC's Negative Option Rule Preempted the Wisconsin Statute as to Time Warner's September 1 Restructuring.

Because it concluded that the FCC's negative option rule was invalid, the district court did not reach the question whether that rule preempted Wis. Stat. § 100.20 as sought to be applied to Time Warner's September 1 restructuring. But the FCC's rule plainly did preempt Wisconsin law.

1. The Wisconsin Statute Conflicted with the FCC's Rule.

Time Warner's Wisconsin restructuring fell squarely within the provision concerning "restructuring or division of tiers of service that do not result in a fundamental change in the nature of an existing

service or tier of service". 47 C.F.R. § 76.981. As previously noted, the FCC expressly determined that it is not an impermissible negative option for a cable operator to remove a service from a regulated tier and offer it on an unregulated a la carte basis. *See* Report and Order ¶ 441 n.1105 ("We also do not believe that anything in the Act requires us to restrict movement of a channel to premium and deregulated status."). As the FCC also recognized, "restructuring of tiers and equipment, including restructuring appropriate for implementing the Cable Act's provisions, will not bring the negative option billing provision into play if subscribers will continue to receive the same number of channels and the same equipment". Report and Order ¶ 441. Because Time Warner's Wisconsin subscribers continued to receive "the same number of channels and the same equipment", there was no "fundamental change",[17] and Time Warner's restructuring was well within the scope of the rule.

Because Time Warner's restructuring was thus expressly permitted under the FCC's negative option rule, the Wisconsin statute (as construed by the Attorney General) was in direct conflict with Federal law and was, therefore, preempted. *See, e.g., Hines v. Davidowitz*, 312 U.S. 52, 67 (1941) (state law preempted if it "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress"); *see also Free v. Bland*, 369 U.S. 663, 666 (1962) ("any state law, however clearly within a State's acknowledged power, which interferes with or is contrary to federal law, must yield"); *accord Kroog v. Mait*, 712 F.2d 1148, 1154 (7th Cir. 1983) (holding state securities law preempted by Federal Arbitration Act because of conflict between state and Federal law), *cert. denied*, 465 U.S. 1007 (1984).

Further, where Federal law authorizes different courses of conduct, the Supremacy Clause forbids the states to foreclose one of

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[17] As a matter of law, Time Warner's restructuring could not be considered a "fundamental change" within the meaning of the rule. As an example of a change that it would regard as "fundamental", the FCC mentioned the deletion of all existing channels from a particular tier of service and the addition of "a completely new set of channels". Report and Order ¶ 440 n.1100.

the options that Federal law has permitted. *E.g. Fidelity Federal Savings & Loan Association v. De la Cuesta*, 458 U.S. 141, 155 (1982). Here, the FCC authorized cable operators to restructure their service without resoliciting subscriber orders if they wished, so long as no "fundamental change" occurred.[18] Because the Wisconsin statute purports to hinder or prohibit such a course of action, it is necessarily preempted. *See, e.g., De la Cuesta*, 458 U.S. at 155; *see also Hines v. Davidowitz*, 312 U.S. at 67; *American Agriculture Movement v. Board of Trade*, 977 F.2d 1147, 1156-57 (7th Cir. 1992).

2. The FCC Intended to Preempt State Law to Facilitate Restructuring on September 1.

The FCC made plain that it intended to preempt state laws concerning negative options, and to do so completely insofar as such laws might bear on tier restructuring in connection with the implementation of rate regulation taking place on September 1, 1993. In its initial Report and Order on rate regulation, the FCC rejected the argument, advanced by some municipalities, that state and local governments retained the right to regulate more stringently those practices that might constitute negative options. The Commission stated:

> "Some municipalities argue that state and local governments should have concurrent enforcement powers over negative option billing practices. Austin Comments at 71-72. We do not preclude state and local authorities from adopting rules or taking enforcement action relating to basic services or associated equipment *consistent with the implementing rules we adopt. . . .*" Report and Order ¶ 439 n.1095 (emphasis added).

[18] In certain of its smaller Wisconsin systems, Time Warner did resolicit subscriber orders, as the defendants pointed out below. *See* Affidavit of Judith Stockowitz, sworn to January 7, 1994, Exhibit A. That Time Warner engaged in such resolicitation in some instances does not mean that it was required to do so in all instances. As noted in the text, the FCC's rule created a choice. Operators could resolicit—or not—as they saw fit.

Thus, as a general matter, state and local authorities could pursue negative option issues only with respect to basic services, and only in a manner consistent with the FCC's negative option rule.

As to cable operators' initial tier restructuring to come into compliance with rate regulation requirements on September 1, 1993, the FCC explicitly stated that it intended to preempt any and all state negative option regulation. In its First Order on Reconsideration, the Commission affirmed that "franchising authorities may not regulate tier restructuring in a manner that is inconsistent with the 1992 Cable Act". First Order on Reconsideration ¶ 86 n.127. It went on to add: "In particular, local authorities are precluded from regulating negative option billing to prevent tier restructuring regardless of how the local requirement is characterized". *Id.*

No conclusion can be drawn from these FCC rulings but that the FCC intended to preempt any application of state negative option rules in the context of the September 1 restructuring.[19] As the Supreme Court has stated, "if the FCC has resolved to pre-empt an area of cable television regulation and if this determination 'represents a reasonable accommodation between conflicting policies' that are within the agency's domain", then "we must conclude that all conflicting state regulations have been precluded". *Crisp*, 467 U.S. at 700 (quoting *Shimer*, 367 U.S. at 383). A reviewing court "should not disturb" the FCC's preemption decision unless it reflects a policy "accommodation" that "is not one that Congress would have sanctioned". *City of New York v. FCC*, 486 U.S. 57, 64 (1988) (quoting *Shimer*, 367 U.S. at 383). Because, as shown above, the policy accommodation reflected in the FCC's negative option rule was well within the agency's power to adopt, its rule preempts state law.

[19] Certainly the Wisconsin authorities proceeded on that basis. Indeed, in the proceedings below they *conceded* that the FCC had intended to preempt state law. *See* Memorandum of Defendant James E. Doyle in Opposition to Plaintiff's Motion for Summary Judgment, dated January 14, 1994, at 9 (arguing that FCC exceeded its authority by its "attempts" to "prohibit defendant's consumer protection enforcement efforts").

Although it did not purport to decide the issue, the court below suggested that the FCC's negative option rule could not have preemptive force under 47 U.S.C. § 552(c)(1), which provides that "[n]othing in this subchapter shall be construed to prohibit any State or any franchising authority from enacting or enforcing any consumer protection law, to the extent not specifically preempted by this subchapter", reasoning (again in a fashion not briefed or argued by either side) that under that provision an FCC regulation could have preemptive force only if the *text of the regulation* so provided. *See* Opinion at 18, A13 (text of FCC regulation "contains nothing that can be said to preempt Wisconsin's enforcement action specifically").

On its face, however, § 552(c)(1) does not purport to place any limit on the FCC's authority. It merely makes clear that Congress did not intend to "occupy the field" of consumer protection so broadly in the cable area as to oust all state power by implication, *see, e.g.*, *Rice v. Santa Fe Elevator Corp.*, 331 U.S. 218, 234 (1947), an inference that otherwise would have been quite reasonable, considering the comprehensive regulatory scheme Congress envisioned and authorized. Courts have repeatedly held that validly adopted regulations of administrative agencies can preempt state law, and such decisions do not require that a preemptive intent be expressed in the text of the regulation. *See, e.g.*, *City of New York*, 486 U.S. at 65 (state law held preempted based on FCC commentary in Report and Order promulgating rule); *accord De la Cuesta*, 458 U.S. at 153-54 (noting that the intent of Congress to preempt may be implied from the "structure and purpose" of a statute, and declaring that "[f]ederal regulations have no less preemptive effect than federal statutes"). The district court's suggestion that preemptive intent must be codified in FCC regulations should be rejected.

C. The FCC's Recent Third Order on Reconsideration Does Not—and Cannot—Alter This Analysis.

As noted at the outset, in its Third Order on Reconsideration the FCC has recently revisited the subject of preemption of state negative option laws. It has acknowledged that its earlier discussions (*see* Report and Order ¶ 439 n.1095; First Order on Reconsideration ¶ 86 n.127) "may be construed as attempting to preempt states and local franchising authorities from regulating negative option billing in a manner inconsistent with our rate regulation rules generally and our

specific rule addressing negative option billing". Third Order on Reconsideration ¶ 125. Acting "on reconsideration on our own motion", however, the FCC has determined to "substitute" a new analysis "in place of the two statements in our previous orders" referenced above. *Id.* ¶ 126. The gist of the new analysis is that "[s]tate and local government jurisdiction to regulate negative option billing under consumer protection laws is concurrent with the Commission's jurisdiction to regulate negative option billing under the Communications Act". *Id.*

The FCC's "substituted" discussion of the preemptive force of its negative option regulation was not intended to change, retroactively, the preemptive force of that regulation with respect to tier restructuring on September 1, 1993. The FCC declared that its Third Order on Reconsideration would not go into effect until May 15, 1994. *Id.* ¶ 159. Where an administrative agency delays the effective date of its action, the action should not be applied retroactively. *See Criger v. Becton*, 902 F.2d 1348, 1351 (8th Cir. 1990) (delayed effective date "is evidence that cuts against retroactive application"); *see also* 2 Norman J. Singer, *Sutherland Statutory Construction* § 41.04 (5th ed. 1992) ("postponement of the effective date for an act indicates that it should have only prospective application").

In any event, the FCC could not retroactively alter the preemptive force of its negative option regulation with respect to cable operators' September 1, 1993, restructuring even if it wished to do so. As set forth above, both the regulation and the FCC's commentaries on it were issued on the eve of the implementation of rate regulation pursuant to the 1992 Cable Act and the FCC's regulations. There can be no doubt that Time Warner and other cable operators relied upon them, and that the FCC intended such reliance. To retroactively reverse the rules under which Time Warner (and other cable operators across the United States) conducted their restructuring would be impermissible under well-settled principles.

First, because "[r]etroactivity is not favored in the law", an administrative agency's "statutory grant of legislative rulemaking authority will not, as a general matter, be understood to encompass the power to promulgate retroactive rules unless that power is conveyed by Congress in express terms". *Bowen v. Georgetown*

University Hospital, 488 U.S. 204, 208 (1988); *see also Landgraf v. USI Film Products*, 114 S.Ct. 1483, 1501 (1994) (Supreme Court has "long embraced a presumption against statutory retroactivity"). Nothing in § 3 of the 1992 Cable Act authorizes the FCC to engage in retroactive rulemaking, and, as a general matter, it would appear that the FCC lacks such power. *See, e.g., ICORE, Inc. v. FCC*, 985 F.2d 1075, 1080 (D.C. Cir. 1993) (FCC concedes it lacks authority to promulgate retroactive rules).

Second, "[a]lthough an administrative agency is not bound to rigid adherence to its precedents, it is equally essential that when it decides to reverse its course, it must give notice that the standard is being changed" and must "apply the changed standard only to those actions taken by parties after the new standard has been proclaimed as in effect". *Boston Edison Co. v. FPC*, 557 F.2d 845, 849 (D.C. Cir.), *cert. denied*, 434 U.S. 956 (1977); *accord RKO General, Inc. v. FCC*, 670 F.2d 215, 223-24 (D.C. Cir. 1981) (same). As this Court has put it, "[w]hen an agency waffles without explanation, taking one view one year and another the next", or "gets out the Dictionary of Newspeak and pronounces that for purposes of its regulation war is peace", then, at a minimum, "notice, an opportunity for comment, and an adequate record" are required. *Homemakers North Shore, Inc. v. Bowen*, 832 F.2d 408, 412 (7th Cir. 1987). Here, where the FCC has acted "on reconsideration on our own motion", without any notice or opportunity for comment, its new standard is probably invalid even prospectively.

Third, an agency cannot issue retroactive rules "when to do so would lead an individual or group who had relied on the government's previous position to forfeit 'legal right[s]' or unduly suffer 'any adverse change in its status'". *Motion Picture Ass'n of America, Inc. v. Oman*, 750 F. Supp. 3, 10 n.7 (D.D.C. 1990), (quoting *Heckler v. Community Health Services of Crawford County, Inc.*, 467 U.S. 51, 61-62 (1984)), *aff'd*, 969 F.2d 1154 (D.C. Cir. 1992). Here, Time Warner and many other cable operators have relied upon the FCC's pronouncements in determining how to restructure their cable services. To change those rules retroactively would obviously impair Time Warner's rights.

Accordingly, whatever the FCC's views on the preemptive force of its negative option rule as applied in the future, that rule preempted

Wis. Stat. § 100.20 as applied to Time Warner's September 1, 1993 restructuring.

II. THE THREATENED APPLICATION OF § 100.20 CONSTITUTES IMPERMISSIBLE STATE REGULATION OF CABLE RATES

Section 3 of the 1992 Cable Act provides that "no Federal agency *or State* may regulate the rates for the provision of cable service except to the extent provided under this section". 47 U.S.C. § 543(a)(1) (emphasis added). As the district court recognized, under that provision, "Wisconsin is precluded from regulating cable rates". (Opinion at 18, A14) The district court held, however, that application of Wis. Stat. § 100.20 to Time Warner's restructuring would not constitute improper rate regulation because Time Warner would have the option of not providing the a la carte services to any person who did not affirmatively order them. (Opinion at 19, A15) Although the court below found Wisconsin's request for "disgorgement" pursuant to the state law "slightly more problematic", it concluded that the prohibition of rate regulation was not implicated because Wisconsin could have imposed a fine equal in amount to the amount of revenues received from the a la carte services. (Opinion at 20, A15) The district court's analysis was wrong on all counts.

In the first place, both Congress and the FCC considered the negative option provision to be an integral feature of rate regulation. Congress placed the negative option provision in 47 U.S.C. § 543, which is entitled "Regulation of Rates". This placement of the provision shows that Congress regarded the regulation of negative options as an aspect of rate regulation. *See, e.g., Hardin v. City Title & Escrow Co.*, 797 F.2d 1037, 1039 (D.C. Cir. 1986) (section headings and the placement of provision within statute provide evidence of congressional intent); 2A Norman J. Singer, *Sutherland Statutory Construction* § 47.14 (5th ed. 1992) ("[w]here headings are enacted as a part of an act" they "may serve as an aid to the legislative intent"). Although the FCC has recently suggested that negative option issues often may not implicate rate regulation concerns, *see* Third Order on Reconsideration ¶¶ 128-131, its Report and Order treat the negative option provision as an integral part of rate regulation, addressing negative option issues repeatedly, *see* Report and Order ¶¶ 433-442, ¶¶ 448-455.

The district court refused to ascribe any significance to the placement of the negative option provision in the rate regulation section of the statute or to the FCC's treatment of negative options as an aspect of its rate regulation proceeding. The court reasoned that "such congressional and agency actions", although possibly "relevant to ascertaining congressional intent", here "may demonstrate nothing more than that Congress recognized that disputes over alleged negative option billing practices would arise in connection with rate regulation-induced restructuring". (Opinion at 21, A16) The court concluded that "these possible indications of congressional intent" were "not strong enough to overcome the presumption against preemption".

Even if there were a "presumption" against preemption,[20] the district court's analysis completely missed the point. Section 3 of the 1992 Cable Act itself overcomes any such "presumption", for it *expressly ousts the states of any role in regulating cable rates*, as the court elsewhere acknowledged (*see* Opinion at 18 n.4, A14 n.4). The question was whether Congress regarded its prohibition of negative options as an aspect of rate regulation. The nature of the negative option provision and Congress's placement of it in the rate regulation section of the Act, as well as the FCC's treatment of it, were, as the district court conceded, "relevant in ascertaining congressional intent" on this score (Opinion at 21, A16), and they show that Congress did view that provision as an integral part of rate regulation.

Furthermore, although the district court stressed that courts are required "to acknowledge the real world context of the cases before

[20] For the existence of such a "presumption", the court below cited *Rice v. Santa Fe Elevator Corp.*, 331 U.S. 218, 230 (1947), for the proposition that the "historic police powers" of the States are "not to be superseded" unless "that was the clear and manifest purpose of Congress". (Opinion at 21, A16) The Supreme Court has held, however, that "the relative importance to the State of its own law is *not material* when there is a conflict with a valid federal law, for the Framers of our Constitution provided that the federal law must prevail". *Free v. Bland*, 369 U.S. at 666 (emphasis added); *accord De la Cuesta*, 458 U.S. at 153.

them even when the often technical process of construing a statute is at issue" (Opinion at 20, A15), it in fact construed the statute here in a vacuum, without regard to the practical realities of implementing restructuring under a complex and untested framework in an exceedingly short (and recently abbreviated) period of time. The proposed application of Wis. Stat. § 100.20 would not have permitted Time Warner to charge any subscriber for any unbundled a la carte service, unless it first obtained a re-confirming order for the service. Under the state statute (as construed by the Attorney General), Time Warner would have been required either to take steps to discontinue providing the services to subscribers without any meaningful notice to them, and to do so at a time when subscriber satisfaction was already at risk because of many dislocations associated with implementing the statutory scheme, or else to provide the services free of charge until it was able to contact all subscribers and complete the resoliciting process.

Such an application of the state law would amount to a state-mandated rate freeze and would effectively set rates for the a la carte services at zero. It is no answer to say, as the district court suggested (Opinion at 19, A14), that Time Warner could avoid this dilemma simply by refraining to offer the a la carte services to subscribers. By such reasoning, Wisconsin could regulate any rates for cable service that it wished—for the operator could always avoid such regulation simply by refraining from providing the service.[21] Once again,

[21] In this connection, the court cited three decisions made under the Cable Communications Policy Act of 1984 (the "1984 Cable Act"), which the 1992 Cable Act amended and, in many respects, superseded. *See* Opinion at 19, A14, citing *Cable Television Association v. Finneran*, 954 F.2d 91 (2d Cir. 1992); *Storer Cable Communications v. City of Montgomery*, 806 F. Supp. 1518 (M.D. Ala. 1992); *Comcast Cablevision of Sterling Heights, Inc. v. Sterling Heights*, 443 N.W. 2d 440 (Mich. App. 1989). Those cases, however, are inapposite. Under the 1984 Cable Act, cable rates were generally deregulated—no one could regulate them. *Finneran*, *Comcast* and *Storer* all evince some tendency to construe the concept of rate regulation narrowly under the 1984 Cable Act in order to permit some form of rate regulation. In contrast, the 1992 Cable Act establishes

Congress and the FCC sought to encourage unbundling; where the Wisconsin law, as sought to be enforced by the Attorney General, would stand as an impediment to Congress's goals, the Federal law prevails. *De la Cuesta*, 458 U.S. at 155.

Similarly, the fact that Wisconsin might have sought to levy fines instead of seeking "disgorgement" of all of the revenues previously received by Time Warner for the a la carte services is immaterial. Wisconsin has not given itself the power to impose such fines. *See* Wis. Stat. § 100.26. Moreover, the question is not what the state might have done, but what it tried to do.[22] In fact, a refund of rates previously paid is one of the remedies contemplated under the rate regulation regime of the 1992 Cable Act. *See, e.g.*, 47 U.S.C. § 543(c)(1)(C) (authorizing FCC to order refund of "unreasonable" rates). The fact that Wisconsin has attempted to invoke such a remedy merely highlights the extent to which it is attempting to engage in improper rate regulation. *See Nashoba Communications Limited Partnership No. 7 v. Town of Danvers*, 703 F. Supp. 161, 165 (D. Mass. 1988) (rate freeze constitutes impermissible rate regulation), *rev'd on other grounds*, 893 F.2d 435 (lst Cir. 1990); *Town of Norwood v. Adams-Russell Co.*, 406 Mass. 604, 612-13, 548 N.E.2d 1115, 1119 (1990) (same).

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a broad rate regulation regime, so that any concern manifested in those decisions about permitting cable operators to operate in a regulatory vacuum as to their rates now lacks any force.

[22] As indicated by the district court's opinion, when the matter was being litigated below, the parties were in the process of negotiating a stipulation governing their conduct during the pendency of this litigation, pursuant to which (among other things) the request for disgorgement would be dropped from the prayer for relief in the Administrative Complaint. Such an agreement is in the process of being finalized between the parties. This development does not, however, alter the analysis presented in the text.

CONCLUSION

For the reasons stated above, the judgment appealed from should be reversed, and the matter should be remanded with instructions to enter judgment in favor of Time Warner declaring that Wis. Stat. § 100.20 has been preempted with respect to Time Warner's September 1, 1993 restructuring of its Wisconsin cable service and enjoining defendants from attempting to enforce § 100.20 with respect to such restructuring.

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